Supreme Court, U. S.
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IN THE

Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-1521

COVINGTON FABRICS CORP., APPELLANT,

versus

SOUTH CAROLINA TAX COMMISSION, APPELLEE

ON APPEAL FROM THE SOUTH CAROLINA SUPREME COURT

JURISDICTIONAL STATEMENT

JAMES M. WINDHAM,
Post Office Box 11386,
Columbia, South Carolina,
Counsel for Covington
Fabrics Corp., Appellant.

The R. L. Bryan Company, Legal Printers, Columbia, S. C.

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COVINGTON FABRICS CORP., APPELLANT,

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SOUTH CAROLINA TAX COMMISSION, APPELLEE

ON APPEAL FROM THE SOUTH CAROLINA SUPREME COURT

JURISDICTIONAL STATEMENT

INTRODUCTORY PARAGRAPH

Appellant appeals from the judgment of the Supreme Court of the State of South Carolina filed on March 10, 1975, affirming an Order of the Court of Common Pleas which held that Appellant was liable for South Carolina additional corporate income taxes and corporate license fees. This statement is submitted to show that the Supreme Court of the United States has jurisdiction of the appeal and that substantial questions are presented.

OPINION BELOW

The Supreme Court of South Carolina filed a written opinion, which is not yet officially reported, but is unofficially reported at 212 S. E. (2d) 574, the text of which is set out in Appendix A, *infra,* at page 17. The Court of Common Pleas Order, which is unreported, is set out in Appendix B, *infra,* at page 24. Report of Master in Equity, which is unreported, is set out *infra* as Appendix C, at page 30.

JURISDICTION

The decision from which this appeal is taken is the final judgment of the highest Court of the State of South Carolina. Jurisdiction of this Court is invoked pursuant to 28 U. S. C. 1257(2). This appeal draws into question the applicability of South Carolina Code of Laws of 1962, as amended, § 65-222.2, § 65-279.6, § 65-602, and § 606 on the ground that as applied they are repugnant to the U. S. Constitution and *contra* to Federal law.

On December 23, 1969, Appellant, doing a multi-state business, paid South Carolina corporate income taxes and corporate license fees (dependent upon income tax liability) assessed by Appellee for the years 1964 through 1968 and timely brought suit to recover the same. Appellant contended that the allocation of sales to it by the Appellee did not bear a reasonable relation to the proportion of trade or business carried on in or to the benefits conferred by the State of South Carolina; that there was an undue burden on interstate commerce in violation of Article 1, Section 8, of the Constitution of the United States, in violation of Section 1 of the Fourteenth Amendment to the Constitution of the United States in that it was a taking without due process of law, and the extent of activity of Appellant in the states of the purchasers of its goods removed the protection of Federal law, to wit, Public Law 86-272 (15

U. S. C., § 381) so as to cause sales to be "taxable" in the state of the purchaser rather than to be claimed as sales by Appellee. In its Opinion filed March 10, 1975, the Supreme Court of South Carolina held that the taxes and license fees allocated by Appellee did not violate the Commerce Clause or the Fourteenth Amendment to the U. S. Constitution and failed to consider evidence showing activity in states of the purchasers to be beyond the protection of Public Law 86-272 (15 U. S. C., § 381) so as to make sales claimed by Appellee "taxable" in those states of the purchasers.

This Court has jurisdiction where a state court holds a state statute to be applicable in face of a contention that such application is invalid on federal grounds. *Bantam Books, Inc. v. Sullivan,* 372 U. S. 58, 83 S. Ct. 631 (1963); *Central R. R. of Pennsylvania v. Commonwealth of Pennsylvania,* 370 U. S. 607, 82 S. Ct. 1297, and *Dahnke-Walker Milling Co. v. Bondurant,* 257 U. S. 282.

In the event that the Court does not consider appeal the proper mode of review, Appellant requests that the papers upon which appeal is taken be regarded and acted upon as a Petition for Writ of Certiorari, pursuant to 28 U. S. C., § 2103.

CONSTITUTIONAL PROVISIONS AND STATUTES INVOLVED

1. The Commerce Clause of the United States Constitution set out in Appendix D hereto.

2. Section 1 of the Fourteenth Amendment to the United States Constitution set out in Appendix E hereto.

3. 15 U. S. C. § 381 (Public Law 86-272) set out in Appendix F hereto.

4. South Carolina Code of Laws (1962) §§ 65-222.2, 65-279(6), 65-602 and 65-606 (the South Carolina corporate

income and license tax provisions) set out in Appendix G hereto.

QUESTIONS PRESENTED

I. In view of the fact that Public Law 86-272 (15 U. S. C. 381) only restricts a state in imposing a tax on net income of a unitary business where the only contact with the taxing state is the mere solicitation of orders therein, can Appellee apportion to itself sales of Appellant's products in states of the purchasers when the uncontradicted evidence shows that the activities of Appellant in such states exceed mere solicitation of orders?

II. Where the activity of Appellant in South Carolina in the mere maintenance of a rented warehouse where its goods are temporarily kept awaiting shipping orders, and, where sales to S. C. customers are only slightly over 1% of all sales, is it just, fair, reasonable or constitutional for Appellee to claim an apportionment made up of 70% of all property, 20% of all payrolls and 84% of all sales, or a total of 55.5% of all Appellant's entire income?

III. Since the decision of *N. W. States Portland Cement Co. v. State of Minn.*, 358 U. S. 450, 79 S. Ct. 357, is it no longer required that the apportionment of income bear a direct relation to the income producing activities, that the portion of the net income taxed arise from those income producing activities, and bear a direct relation to the protection and opportunities afforded by the taxing state?

STATEMENT

A. Material Facts.

The Appellant, Covington Fabrics Corp., is a New York corporation with its headquarters in New York City. It purchases griege goods (raw materials) from abroad and from suppliers in the United States. These raw materials are shipped to one of three completely independent

cleaning and finishing plants to clean and to convert into slipcovers, draperies and upholstery fabrics. One such plant to which a fee is paid by Appellant for the service of cleaning and converting is located in South Carolina, one in Massachusetts, and the third in North Carolina. These fee-paid, independent cleaners and converters ship the converted goods to Appellant's rented warehouse located at McColl, South Carolina to be retained there awaiting shipping orders from Appellant's headquarters in New York. Appellant's rented warehouse manager and a crew of laborers at McColl, S. C. pack and ship the goods as per New York instructions to purchasers in all fifty states and abroad. Appellant owns no manufacturing plant in South Carolina, has no sales offices here, no showroom, and no executive nor administrative personnel here. The salesman who services South Carolina comes in twice per year for a total of four days per year. All planning, design, pricing, billing, management, inventory and record keeping are done in New York. Appellant maintains sales office, showrooms and a merchandise mart in Chicago and Los Angeles. Sales of Appellant's goods to South Carolina customers are minimal, there being only slightly over one per cent of total sales to South Carolina customers. Appellant's salesmen when they come into a state, in addition to soliciting orders, also have the duty to collect and service delinquent accounts.

Appellant allocated to South Carolina 70% of all property, 20% of all payrolls, and slightly over 1% of all sales. Appellant voluntarily paid to Appellee corporate income taxes and corporate license fees based on the aforesaid allocation, thus allocating to Appellee some 29% of Appellant's entire income. Appellant actually paid taxes on its income to New York and California in addition to South Carolina.

Appellee assessed additional income taxes and corporate license fees, accepting the 70% allocation of all property, the 20% allocation of all payrolls, but raised the sales allocation to 84% of all sales, accomplishing this by claiming sales made to purchasers in other states where those states had not "taxed," asserting that those sales were not "taxable" in the state of the purchaser, and, therefore, were sales which Appellee could claim under South Carolina Code of Laws (1962) §§ 65-279(6) and 65-222.2, Appendix G hereto. After laying claims to such sales, Appellee had allocated to itself 55.5% of Appellant's entire income.

B. Stage at which Federal Questions Raised.

When Appellee gave notice of the proposed additional taxes and license fees, the Federal questions were raised by Appellant. They were raised in the pleadings filed in the Court of Common Pleas. They continued to be raised in the hearings before the Master in Equity of Richland County to whom the Judge of the Court of Common Pleas referred the matter, whose Report is set out, *infra,* as Appendix C, in Exceptions taken to that Report, in the Court of Common Pleas on the Exceptions to the Master's Report and before the Supreme Court of South Carolina, where the Federal constitutional questions were briefed and argued, as well as the matter of the misapplication of Public Law 86-272 (15 U. S. C. 381). The Supreme Court of South Carolina stated "* * * the application of the three factor formula does not produce a result that is in conflict with the Constitutional provisions referred to nor does the application of the formula depart from the requirement of Section 65-222.2 of the Code."

The said Court further stated with reference to Public Law 86-272 (15 U. S. C. 381): "This act of Congress requires minimum contact and activity within a state by a foreign corporation before its income can be taxed by the

state and therefore inferentially, if not directly, limits the application of the sales factor found in Section 65-279.6. Such is not relevant in this action however because the evidence supports one conclusion, that being that the corporation in these periods was taxable only in three states: New York, California and South Carolina." Appendix G, *infra,* page 43.

The appellant took the position that the additional income taxes and corporate license fees were unconstitutionally assessed and collected and that the activities of Appellant in states of the purchasers of Appellant's goods supported a tax, that the income was "taxable" there because of the testimony that showed activity in excess of the protected minimum activity, that the criterion was not whether such income "had been taxed" but rather whether in light of Public Law 86-272 (15 U. S. C. 381) such income was "taxable" in the state of the purchaser.

THE QUESTIONS ARE SUBSTANTIAL

The opinion of the South Carolina Supreme Court being appealed sanctions the assessing and collecting of corporate income taxes and license fees from a foreign corporation engaged in a unitary or multistate business by including, in the sales factor of its three factor formula, sales of goods shipped from Appellant's rented warehouse in South Carolina to purchasers in other states, where the uncontradicted testimony was that the extent of the activity of Appellant's salesmen in all states where its goods were sold (being all fifty states) exceeded the minimum *nexus* or contact protected by 15 U. S. C. 381 (Public Law 86-272). By so sanctioning the Supreme Court of South Carolina has ignored the matter of whether such sales were "taxable" and has merely determined that if such sales were not, in fact, "taxed" in the state of the purchaser, then such sales were not "taxable" in such states and, thus, despite

minimal sales in South Carolina, Appellee can pad its apportionment of sales by picking up all sales where they were not "taxed" in the state of the purchaser. The decision of the South Carolina Supreme Court on this point, that is, in its interpretation and application of Federal law, 15 U. S. C. § 381 (Public Law 86-272), is in direct conflict with decisions of the highest court of Oregon in *Herff Jones Co. v. State Tax Commission* (Oregon, 1967), 430 P. (2d) 998, and the highest court of Arkansas in *Hervey v. A. M. F. Beaird* (Ark. 1971), 464 S. W. (2d) 557, both of which courts gave a narrow construction to Public Law 86-272 (15 U. S. C. § 381), and holding that its purpose was to restrict the right to tax only in cases involving contact with such state to merely solicit orders, and that activity beyond that in such state rendered the taxpayer "taxable" therein. Equally involved and equally substantial is the Federal question whether with its contact with South Carolina the mere maintenance of a rented warehouse to which its goods are temporarily sent awaiting instructions from Appellant's headquarters in New York, a function formerly handled by "drop shipments" on the part of independent cleaners and converters, it is unconstitutional to exact, as Appellee's proper share, a tax based on 70% of property, 20% of payroll and 84% of sales in that such allocation is a taking of property without due process of law and an undue burden on interstate commerce. There are substantial Federal questions in light of decisions of this Court in *Norfolk and Western Railway Co. v. North Carolina,* 297 U. S. 682, 56 S. Ct. 625, holding that a formula which is not arbitrary or unconstitutional on its face, or in general application, might be unfair and unreasonable when applied to a particular state of facts. Appellant has contended that the sales factor formula, as applied, in that it encompasses "sales" that were "taxable" in the state of the purchaser

of Appellant's goods, has resulted in a taking of property without due process and an undue burden on interstate commerce. These are substantial questions.

I. South Carolina cannot apportion to itself sales of Appellant to purchasers in other states where the activity (contact) of Appellant in those states exceed the mere solicitation of orders.

If the decision of the Supreme Court of South Carolina is correct and allowed to stand, then, it means that whether or not the activity of such multi-state unitary business in South Carolina is minimal, as here, nevertheless, even in the maintenance of a rented warehouse, in which its goods are temporarily housed awaiting sales orders from outside South Carolina, Appellee can justify an unconstitutional allocation by examining to see in how many states of purchasers income has been "taxed" and claiming as its own, untaxed income. Such a situation does not insure fair, reasonable and constitutional apportionment, but, to the contrary, fosters a means whereby the exaction by Appellee has no reasonable relation to the activity in or the extent of protection and opportunities afforded by maintenance of a rented warehouse in South Carolina. It is the intent of Public Law 86-272 (15 U. S. C. § 381) that if activity or contact by a corporation engaged in interstate commerce in a particular state is beyond the mere solicitation of orders therein, then, the protection against that state's asserting a tax on income is lost and the income is "taxable" in that state. A decision by this Court settling this issue is imperative.

Several states through decisions of their highest courts, *supra,* have held that protection against taxation provided by Public Law 86-272 (15 U. S. C. § 381) is lost when something more is done than to merely solicit orders

by incoming salesmen in a state by one engaged in interstate commerce.

In enacting Public Law 86-272 Congress intended to free interstate commerce from compliance with diverse, dissimilar, inconsistent and overlapping state income tax laws. [S. Rep. No. 658, 86th Congress, 1st Session, 2-5 (1959).] To get that result proper and uniform interpretation thereof is paramount.

Appellant produced testimony, which was uncontradicted, that the activity of its salesmen coming into the 50 states in which sales were made exceeded the mere solicitation of orders. (Tr. ff. 225, 241-243.) They regularly engaged in collecting and serving delinquent accounts.

II. Where the activity of Appellant in South Carolina is the maintenance of a rented warehouse and where sales to South Carolina customers are only slightly over 1% of all sales, it is not fair, just, reasonable or constitutional to demand an allocation of 70% of all property, 20% of all payroll, and 84% of all sales.

Appellant produced testimony, which was uncontradicted, that the rented warehouse at McColl, S. C. represents no capital investment [Tr. ff. 455-457] and that this only contact with South Carolina (the rented warehouse) could be abandoned promptly with no disruption to its business [Tr. ff. 469-471]. This demonstrates conclusively the lack of any real part that this rented warehouse plays in the production of income and also points out the minimum protection and opportunities afforded Appellant by South Carolina.

This Court has made numbers of decisions in cases dealing with the right of a state to tax income of a business the components of which are carried on in several states. Those decisions uniformly sanction a tax on net income provided the tax bears a reasonable relation to the activity

of the interstate business within the taxing state. At the same time this Court has uniformly held that in the absence of such logical and reasonable reference to the production of income within the taxing state, then it comes into conflict with the Fourteenth Amendment. *Maxwell v. Kent-Coffey Mfg. Co.*, 204 N. C. 365, 168 S. E. 397, aff. 54 S. Ct. 437.

In *Ott v. Mississippi Valley Barge Line*, 366 U. S. 169, 69 S. Ct. 432, it was held that the tax in its practical operation must be related to the opportunities, benefits and protection afforded by the taxing state and that requirement is satisfied if the tax is fairly apportioned to the commerce carried on within the state. It goes without saying that this taxpayer's being able to abandon all taxable contact with South Carolina with no disruption of business there cannot possibly be any opportunities, benefits and protection afforded by South Carolina justifying an apportionment made up of 70% of all property, 20% of all payroll and 84% of all sales.

III. This Court in N. W. States Portland Cement Co. v. State of Minn., 358 U. S. 450, 79 S. Ct. 357, a landmark decision in area of taxation of interstate operations, specifically left open the matter of fairness of apportionment, stating that issue not involved.

Following this decision, Congress passed Public Law 86-272 (15 U. S. C. 381) to specifically protect a foreign corporation from state taxation of its interstate income where the only contact with such state was the visitation therein by taxpayer's salesmen to solicit orders. However, in the said decision itself, without regard to the later enactment, this Court implicitly recognized that the bare right to taxation and the fairness of the exaction were two entirely different things. The Court stated "where taxes imposed by a state on the income of a foreign corporation are

levied only on that portion of the corporation's net income which arises from its activities within the taxing state, and the corporation engages in substantial income-producing activity in the taxing state, imposition of the tax does not contravene the Due Process Clause of the Federal Constitution."

Appellant has shown by direct evidence that it did not engage in substantial income-producing activity in South Carolina, and that to tax 84% of all its sales is to tax far beyond that portion of its net income arising from its activities (the renting of a warehouse in which its goods are temporarily kept) within South Carolina.

The decision of the South Carolina Supreme Court, Appendix A, *infra*, herein, carries the decision of this Court in *N. W. Portland Cement Co. v. State of Minn.*, 358 U. S. 450, 79 S. Ct. 357, a case dealing with *nexus*, the bare right to tax, far beyond that point to the point of the fairness of the apportionment, and must be construed to mean that any contact, however small, justifies an apportionment to Appellee of 55.5% of Appellant's entire net income.

In *N. W. Portland Cement, supra*, this Court carefully pointed out that the reasonableness of the apportionment of net income was not involved.[1] The fairness of the formula is the sole issue raised throughout by Appellant here.

Research has failed to disclose any case decided by the Supreme Court of South Carolina involving the fairness of the specific there factor formula as applied to an interstate business.

There have been several decisions by that Court involving which formula, that is, a two factor formula or a three factor formula, was the proper of two available formulae in terms of the nature of the taxpayer's business.

[1] At page 359 of the reported case, it is stated "No question is raised in either case as to the reasonableness of the apportionment of net income under the State's formulas nor to the amount of the final assessment made."

Additionally, research has failed to disclose any decision where the proven activity was so minimal and the exaction, in turn, so extremely unreasonable.

This Court has recognized that where activities within a taxing state do not have a real and substantial relation to the business transacted therein, there are resulting constitutional violations, and, in *Wisconsin v. J. C. Penney Co.*, 311 U. S. 435, 61 S. Ct. 246, the Court stated that "Attempted transgressions of these limits of state sovereignty have time and time again run afoul of the Fourteenth Amendment." Here, there is a positive showing by Appellant that Appellee has overstepped those limits.

CONCLUSION

For the foregoing reasons, this Court should note probable jurisdiction and reverse the judgment below.

Respectfully submitted,

JAMES M. WINDHAM,
Counsel for Appellant,
Covington Fabrics Corp.

APPENDIX

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APPENDIX A

The State of South Carolina
IN THE SUPREME COURT

COVINGTON FABRICS CORP., APPELLANT,

versus

SOUTH CAROLINA TAX COMMISSION, RESPONDENT

APPEAL FROM RICHLAND COUNTY, JOHN GRIMBALL, JUDGE

OPINION NO. 19968
Filed March 10, 1975

AFFIRMED

HERBERT, DIAL & WINDHAM,
Columbia, S. C.,
Attorneys for Appellant.

DANIEL R. McLEOD,
Attorney General,

JOE L. ALLEN, JR.,
Assistant Attorney General,

G. LEWIS ARGOE,
Assistant Attorney General,

JOHN C. VON LEHE,
Assistant Attorney General,
Columbia, S. C.,
Attorneys for Respondent.

MOSS, C. J.: Covington Fabrics Corporation, the Appellant herein, brought this action against the South Carolina Tax Commission, the Respondent herein, pursuant to Sections 65-2661 and 65-2662, Code of 1962, as amended, to recover the sum of $36,227.32, together with interest

thereon, being additional corporate income taxes and corporate license fees assessed by the Respondent against the Appellant. The taxes so assessed were paid under protest on December 23, 1969.

The Respondent, by way of answer, alleged that the additional income taxes and corporate license fees were properly assessed pursuant to the sales factor contained in the tax apportionment formula. Sections 65-279.3 through 65-279.6 of the Code.

This case was referred to the Master in Equity for Richland County, and he was directed to take the testimony and to report his findings of fact and conclusions of law. The Master recommended that the claim of the Appellant be denied. The Appellant filed numerous exceptions to the Master's Report, and these were heard by the Honorable John Grimball, Resident Judge, who, by his order of January 12, 1974, confirmed the Report of the Master. This appeal followed.

The questions to be decided in this case are whether the Respondent properly applied the sales factor of the apportionment formula contained in Sections 65-279.3 through 65-279.6 of the Code and, if such formula was correctly applied, did it produce an unconstitutional result.

The Appellant, a corporation existing under the laws of the State of New York, engages in a unitary business both within and without this State and is therefore subject to income and corporate license taxation by this State.

Income tax returns for the tax period ending May 31, 1967, through May 31, 1969, inclusive, were filed by the corporation, and a tax was paid on net income that had been apportioned by use of a three factor formula consisting of the average of the percentages of property in this State to all property, payroll in this State to all payrolls and sales in this State to all sales. The corporation, in the use of the sales factor, allocated slightly more than one (1%) percent of total sales to South Carolina, those being sales delivered to South Carolina customers. The Tax Commission, on audit, however, allocated to this State all sales shipped from South Carolina into other states in which the

corporation was not subject to taxation, which resulted in assessments for additional income taxes and interest in the amount of $36,227.32 and corporate license taxes and interest in the amount of $480.78. The tax periods for corporate license taxes were those that ended May 31, 1966, May 31, 1967, and May 31, 1968, and the amount of the additional assessment was also ascertained by use of the three factor formula.

Of the three factors used in the formula to determine the corporation's net income and license base subject to taxation by this State, only the sales factor is involved in this action. Section 65-279.3 provides for the use of the three factor formula for this class of business and Section 65-279.6, the sales factor, is as follows:

> "The ratio of sales made by such taxpayer during the income year which are attributable to this State to the total sales made by such taxpayer everywhere during the income year, and for purposes of this article, sales attributable to this State shall be all sales where the goods, merchandise, or property is received in this State by a purchaser, other than the United States Government. In the case of delivery of goods by common carrier, or by other means of transportation, including transportation by the purchaser, the place at which the goods are ultimately received after all transportation has been completed shall be considered as the place at which the goods are received by the purchaser. Direct delivery into this State by the taxpayer to a person or firm designated by a purchaser from within or without the State shall constitute delivery to the purchaser in this State. **Sales are attributable to this State when the property is shipped from within this State** and the purchaser is the United States Government or **the taxpayer is not taxable in the state of the purchaser**. The word 'sales' as used in this article shall be construed to include rentals of tangible personal property the rentals from which are not separately allocated under this article. Such rentals to be attributed to this State if the property is located in this State. Sales of intangible personal property shall

be attributable to this State if the entire income producing activity is within this State, or based on costs of performance the greater proportion thereof is performed within this State." (Emphasis added.)

The underscored language creates the subject of this action because under such these sales are allocated to this State. The Appellant contends, however, that the allocation resulted in an unconstitutional tax prohibited by the Commerce Clause of the Constitution of the United States (Article 1, Section 8); the due process clauses of the Constitution of the United States (Section 1 of the Fourteenth Amendment), and the Constitution of South Carolina (Article 1, Section 5), and Section 65-222.2 of the South Carolina Code of Laws which levies the tax upon a base that reasonably represents the proportion of the corporation's business carried on within this State. With such contention, we however, must disagree.

It is well settled that a state has a right to impose a tax on apportioned income derived from business conducted partly within and without the state.

"* * * it has been established since 1918 that a net income on revenue derived from interstate commerce does not offend constitutional limitations upon state interference with such commerce. The decision of *Peck & Co. v. Lowe,* 247 U. S. 165, 38 S. Ct. 432, 62 L. Ed. 1049, pointed the way." *Portland Cement Co. v. Minnesota,* 358 U. S. 450, 79 S. Ct. 357, 3 L. Ed. (2d) 421, 67 A. L. R. (2d) 1292. See also *Underwood Typewriter Co. v. Chamberlin,* 254 U. S. 113, 41 S. Ct. 45, 65 L. Ed. 165.

Such also has long been recognized by this Court. *Western Union Telegraph Co. v. Query,* 144 S. C. 234, 142 S. E. 509. We there upheld the right to tax net income arising from interstate operations within the State. In the case of *Santee Mills v. Query,* 122 S. C. 158, 115 S. E. 202, we held that:

"The right of a state to levy an income tax upon income derived by nonresidents from property within

the State or from business carried on within the State is settled in the affirmative by the recent decisions of the Supreme Court of the United States in *Shaffer v. Carter,* 252 U. S. 37, 40 S. Ct. 221, 64 L. Ed. 445 and *Travis v. Yale & Towne Mfg. Co.,* 252 U. S. 60, 40 S. Ct. 228, 64 L. Ed. 46." For other cases and comments, see 90 A. L. R. 484 and 67 A. L. R. 1322.

The only change in this area of taxation is that provided by Federal law found in 15 U. S. C. A. 381. This act of Congress requires minimum contact and activity within a state by a foreign corporation before its income can be taxed by the state and therefore inferentially, if not directly, limits the application of the sales factor found in Section 65-279.6. Such is not relevant in this action however because the evidence supports one conclusion, that being that the corporation in these periods was taxable only in three states; New York, California and South Carolina.

The corporation must establish its contention that the statutes impose an unconstitutional tax by "clear and cogent evidence."

"One who attacks a formula of apportionment carries a distinct burden of showing by 'clear and cogent evidence' that it results in extraterritorial values being taxed. See *Norfolk & Western Ry. Co. v. North Carolina,* 297 U. S. 682, 688, 56 S. Ct. 625, 628, 80 L. Ed. 977." *Butler Bros. v. McColgan,* 315 U. S. 501, 62 S. Ct. 701, 86 L. Ed. 991. See also *State Ex Rel. Maxwell v. Kent Coffey Manufacturing Co.,* 204 N. C. 365, 168 S. E. 397, 90 A. L. R. 476, affd. *per curiam* 291 U. S. 642, 54 S. Ct. 437, 28 L. Ed. 1040.

The obvious purpose of the apportionment formula is the determination of income from business activities within this State and is a proper subject for legislative action. *State Ex Rel. Maxwell v. Kent Coffey Manufacturing Co., supra.*

Although exactness in apportionment is desirable, all that is required is a reasonable approximation.

> "Furthermore, this court has long realized the practical impossibility of a state's achieving a perfect apportionment of expansive, complex business activities such as those of appellant, and has declared that 'rough approximation rather than precision' is sufficient. *Illinois Central Ry. Co. v. State of Minnesota,* 309 U. S. 157, 161, 60 S. Ct. 419, 422, 84 L. Ed. 670. Unless a palpably disproportionate result comes from an apportionment, a result which makes it patent that the tax is levied upon interstate commerce rather than upon an interstate privilege, this court has not been willing to nullify honest state efforts to make apportionments." *International Harvester Co. v. Evatt,* 329 U. S. 416, 67 S. Ct. 444, 91 L. Ed. 390, reh. den., 329 U. S. 834, 67 S. Ct. 628, 91 L. Ed. 706.

We have not found a case that supports the corporation's contention that the application of three factor formula unreasonably apportions income, nor has one been called to our attention. The formula has however been considered and approved as a reasonable basis for apportioning income. The Supreme Court of the United States, in the case of *Butler Bros. v. McColgan, supra,* held that:

> "We cannot say that property, payroll, and sales are inappropriate ingredients of an apportionment formula. We agree with the Supreme Court of California that these factors **may properly be deemed to reflect 'the relative contribution of the activities in the various states to the production of the total unitary income,'** so as to allocate to California its just proportion of the profits earned by the appellant from this unitary business." (Emphasis added.)

The Appellant imports or purchases raw materials consisting of greige goods, that are converted into salable products, slip covers, draperies and upholstery fabrics by independent contractors at three plants; one at Allen, Massachusetts; one at Gaffney, South Carolina, and the other at Cherokee, North Carolina. Some of the raw material acquired by the Appellant is imported through the Port of Charleston, and some is purchased directly from

South Carolina sellers; however, the amount of the same is not found in the record. The Appellant's executive offices are located in New York City, and it is at this office that the design, pattern and color scheme for the salable products are set. The three independent contractors finish the raw materials in accordance therewith, and the salable products are shipped to the Appellant's warehouse located at McColl, South Carolina. Ten salesmen call upon corporate customers in forty-nine (49) states, and when an order is given it is forwarded to the New York office and, if accepted, a packing order is prepared and sent to the warehouse at McColl. When the packing order is received in McColl, it is there filled and thereafter delivered to a common carrier for shipment to the purchaser. The billing and collecting for the sale is from the New York office, and the Appellant has sales offices in New York, Illinois and California.

It is conceded that the business is unitary in nature, therefore its income is attributable to all incidents of the business and not to any single activity.

> "That term (unitary) is simply descriptive, and primarily means that the concern to which it is applied is carrying on one kind of business—a business the component parts of which are too closely connected and necessary to each other to justify division or separate consideration, as independent units." *State Ex Rel. Maxwell v. Kent Coffey Manufacturing Co., supra.* See also Words & Phrases, Vol. 43, p. 499, Unitary Business.

During the tax periods involved, approximately seventy (70%) percent of the Appellant's property and seventeen (17%) percent of its payroll were in this State. After allocating the sales shipped into states where the Appellant was not subject to taxation to this State, approximately 55.5% of its income was apportioned to this State, while of its total income only 83% was subject to taxation by all states.

We cannot conclude from the record before us that the allocation of approximately 55.5% of the Appellant's

income to this State is unreasonable and unrelated to business done in this State. The Appellant relies upon the case of *Hans Rees' Sons v. State of North Carolina,* 283 U. S. 123, 51 S. Ct. 385, 75 L. Ed. 879; however, it is not here controlling. We do not find where the corporation has made any effort to break up its business into separate or component elements as was done in that case.

The activities of the Appellant in this State constitute a substantial part of the unitary business and the application of the three factor formula does not produce a result that is in conflict with the constitutional provisions referred to, nor does the application of the formula depart from the requirements of Section 65-222.2 of the Code.

The exceptions of the Appellant are overruled, and the judgment below is,

Affirmed.

LEWIS, BUSSEY, LITTLEJOHN and NESS, JJ., concur.

APPENDIX B

STATE OF SOUTH CAROLINA,
COUNTY OF RICHLAND.

COVINGTON FABRICS CORP., PLAINTIFF,

versus

SOUTH CAROLINA TAX COMMISSION, DEFENDANT

IN THE COURT OF COMMON PLEAS

ORDER

This matter, which involves a suit pursuant to Sections 65-2661 and 65-2662 of the Code for the refund of corporate income taxes and license fees, has been brought before me on exceptions to the report of the Honorable Owens T. Cobb, Jr., Master in Equity for Richland County, which report concludes that the taxes were properly assessed and that no refund should be ordered.

The controversy concerns the result reached by the application of the South Carolina income tax apportionment formula contained in Sections 65-279.3 through 65-279.6 of the Code; more specifically, the result reached by applying Section 65-279.6 which contains the sales factor of the formula. (This formula is also used in apportioning the corporation license fee.) In paragraphs 14 and 15 of the Complaint, the Plaintiff has alleged that the Defendant applied the apportionment formula and that its application produced an "unreasonable tax result". The Plaintiff further alleged in paragraph 16 that the result reached by the application of the formula is in violation of Code Section 65-222.2 and violates both the State and Federal Constitutions. The Master found, after a consideration of the evidence and arguments presented to him, that the result reached by the application of the apportionment formula did not conflict with the provisions of Section 65-222.2 of the Code, nor did it violate the provisions of the State or Federal Constitutions.

The Plaintiff has filed thirty-four (34) exceptions, each of which has been considered. It would serve no useful purpose to discuss the merits of each exception separately. The Plaintiff itself has not so argued them to me. Exceptions 1, 2, 3 and 8 allege error by the Master in failing to make certain fact findings; however, ample fact findings were made by the Master which support his conclusions and I, therefore, find these exceptions to be without merit. Exceptions 7, 9, 10, 12, 14, 15, 16, 17, 18 and 20 relate to the question of whether the result reached by the literal application of the apportionment formula is in violation of the requirements of Section 65-222.2 of the Code which imposes the corporation income tax. The additional assessment in question arose from the inclusion of certain of the Plaintiff's sales in the sales factor of the apportionment formula. These were sales in which shipment was made from McColl, South Carolina, to purchasers located in other states. The Plaintiff has not contended, and does not now contend, that the Tax Commission did not apply the provisions of the apportionment formula contained in Sections 65-279.3 through 65-279.6 of the Code. Instead, the Plaintiff contends that the Commission should not have followed the literal language contained in those Sections;

more specifically, Section 65-279.6 which contains the sales factor of the formula, because in doing so it violated the provisions of Section 65-222.2 of the Code.

Section 65-222.2 states that if a taxpayer is transacting business partly within and partly without this State, the income tax shall be "imposed upon a base which reasonably represents the proportion of the trade or business carried on within this State". The Master held that the result reached by the application of the apportionment formula produced a "reasonable" result within the meaning of Section 65-222.2 of the Code and that Section 65-222.2 is not inconsistent with the apportionment formula. I am in agreement with these findings and adopt them for the reasons stated in his report. I do not agree with the position of the Plaintiff that because of the provisions of Section 65-222.2 the Tax Commission had a duty not to literally apply the provisions of the sales factor of the apportionment formula. On the contrary, the Commission had a duty to apply the formula. The alternative of applying the formula only when the Tax Commission believed the results reached to be "reasonable" is clearly untenable. Such action would result in the formula being applied to some multistate businesses but not others and create discretionary authority in an administrative body where the General Assembly obviously intended none to exist. The Plaintiff has relied on the case of *Colonial Life and Accident Insurance Co. v. S. C. Tax Commission,* 248 S. C. 334, 149 S. E. (2d) 777. There the taxpayer had, in arriving at its South Carolina income, deducted all taxes paid by it in this State. The Tax Commission had denied a portion of this deduction on the basis that certain taxes paid by Colonial in South Carolina were for the benefit of its business operations in other states as well as here. The Court upheld this apportionment of the deduction and stated that Section 65-222.2 gave the Commission the power to prescribe a method of apportionment. There was no specific method of apportionment of the deduction provided by statute. The decision stands for the proposition that where a method of apportionment is not provided by statute, the Tax Commission can adopt a reasonable method by regulation or administrative construction. The decision does not stand for the proposition advanced by the Plaintiff that the Tax Commission need not follow the precise language of the apportionment formula. Any administrative construction or regulation which differed from the statutory mandate of the formula contained in Sections 65-279.3 through 65-279.6 would be void. There is room for administrative interpretation only in the absence of precise legislative directive. See 2 Am. Jur. (2d), *Administrative Law,* Section 248.

As the Master noted, the Legislature has prescribed the method in the apportionment formula of arriving at the portion of the Plaintiff's business which is taxable in this State. He found, and I concur in his finding, that the Plaintiff has substantial activities in this State. It is not the proper function of the courts to enter into a precise calculation of what percentage of the taxpayer's income is to be allocated to this State. It is, however, the proper function of the judiciary to determine whether the method of taxation prescribed by the Legislature violates some provision of either the South Carolina or the United States Constitutions. The Master found that the application of the apportionment formula in this case was not shown to produce an unconstitutional result, and I affirm this holding to which exceptions 19, 21, 22, 23, 24, 25, 26, 27, 28 and 33 have been taken. The Plaintiff operates a unitary business. Its activities in this State both contribute to and are dependent upon the operation of the business outside this State. The United States Supreme Court has recognized the unitary business concept in taxation at least as early as 1897 in the case of *Adams Express Co. v. Ohio,* 165 U. S. 194, 17 S. Ct. 305. The warehousing function of the Plaintiff in South Carolina unquestionably contributes to its over-all profit which is derived from sales to purchasers located in nearly every state in the Country. Contrary to the contention of the Plaintiff, as expressed in exception 7, the record supports the Master's finding that the Plaintiff has substantial contacts with South Carolina other than its centralized warehousing function which is wholly located here. It purchases unfinished goods from sellers lo-

cated in this State and imports a large portion of its raw material through Charleston. The Plaintiff contracts with South Carolina finishing plants for the conversion of these goods.

The question of the constitutionality of the result reached under an apportionment formula has been before the United States Supreme Court on many occasions. The formulas used in these cases are almost as numerous as the cases themselves. The use of the sophisticated three-factor formula, which is employed by South Carolina, has been specifically sanctioned by the Supreme Court in the case of *Butler Brothers v. McColgan,* 315 U. S. 501, 62 S. Ct. 701 (1942). The Master was correct in quoting the following language from the case of *State of Wisconsin v. J. C. Penney Co.,* 311 U. S. 435, 61 S. Ct. 246, in determining whether the application of the formula violates the Due Process Clause of the Federal or State Constitutions:

> "* * *. That test is whether property was taken without due process of law, or, if paraphrase we must, whether the taxing power exerted by the state bears fiscal relation to protection, opportunities, and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return. * * *."

That rule was strongly affirmed in *Northwestern States Portland Cement Company v. Minnesota,* 358 U. S. 450, 79 S. Ct. 357, a case which involved the constitutionality of an income tax. The apportionment formula has produced a result which attributes slightly more than half of the Plaintiff's total income to South Carolina. It is true that the Plaintiff, in the case at hand, has substantial activities in New York City; however, the record fails to disclose that any state has given more protection to the Plaintiff's business activities than South Carolina. With the exception of some sample merchandise, the Plaintiff's goods were never in New York during either the conversion process or during storage as finished products. The Plaintiff does no manufacturing and warehousing is an important part of its business. After a complete review of the

evidence, I find, as the Master found, that the Plaintiff's activities in this State are sufficient to support the tax levied. As stated in the *J. C. Penney* case, this State has exerted its power in relation to opportunities which it has given, to the protection which it has afforded and to the benefits which it has conferred.

The Plaintiff has attempted to show that the result reached under the apportionment formula has worked a burden on interstate commerce. It has relied heavily on the case of *Hans Rees' Sons v. State of North Carolina,* 283 U. S. 123, 51 S. Ct. 385, to show that extraterritorial values have been taxed. In that case the taxpayer demonstrated by a species of separate accounting that income arising from activities within the taxing state was grossly less than that attributed by the primitive single factor formula then employed by North Carolina. The Master found and I affirm his finding that no such showing has been made here. The *Hans Rees* case and its sequel, *Maxwell v. Kent-Coffey Manufacturing Co.,* 204 N. C. 365, 168 S. E. 397, affirmed *per curiam* 291 U. S. 642, 54 S. Ct. 437, are discussed at length in the South Carolina case of *Mercury Motor Express, Inc. v. South Carolina Tax Commission,* 244 S. C. 134, 135 S. E. (2d) 756. The *Kent-Coffey* decision as well as the *Butler Brothers* decision, *supra,* severely restrict the *Hans Rees* rationale and require clear and cogent evidence to impeach, on constitutional grounds, the result reached by an apportionment formula.

The Plaintiff argued to the Master that the South Carolina apportionment formula subjected it to the risks of multiple taxation. It has not pressed this point to me, and it is sufficient to state that the Master was correct in holding that it is not the risk of multiple taxation, but the fact of multiple taxation which must be shown in order to prove that interstate commerce has been burdened.

At the conclusion of the reference, the Defendant, Tax Commission, moved to strike an amendment to the Complaint. The Plaintiff had amended paragraph six of the Complaint to read: "No sales are consummated except in New York **or some other state except South Carolina where sales to customers are slightly over 1% of total sales.**"

Whether the Plaintiff should have been allowed to add the underscored language to the pleadings was discretionary with the Master. Although it appears that the Defendant has abandoned its motion to strike the amendment, in the interest of clarity, the Defendant's motion is specifically denied. The Master held that the question of where sales are consummated is not controlling here. I adopt that holding which is directly supported by the language quoted by him from the recent South Carolina case of *United States Steel Corporation v. South Carolina Tax Commission,* 259 S. C. 153, 191 S. E. (2d) 9.

I, therefore, affirm the Master's holdings that the result reached under the apportionment formula does not conflict with Section 65-222.2 of the Code and that the result does not conflict with the provisions of either the South Carolina or the United States Constitutions. For the foregoing reasons, I am of the opinion that the Complaint in this action should be dismissed, and

IT IS SO ORDERED.

/s/ JOHN GRIMBALL,
Resident Judge,
Fifth Judicial Circuit.

Columbia, South Carolina
January 12th, 1974

APPENDIX C

MASTER'S REPORT: (C. A. No. 4894)

Columbia, S. C., April 23, 1973

To the Presiding Judge of the Court of Common Pleas for Richland County, South Carolina:

I, the undersigned Master, report that pursuant to the Order of Reference granted in the above-entitled case, two references were held, attended by the attorneys of record, the testimony was taken, which is herewith reported, and from the testimony and evidence presented I find and conclude as follows:

1. This is an action brought pursuant to Sections 65-2661 and 65-2662 of the South Carolina Code of Laws for

the recovery of corporation income taxes and corporation license fees and interest paid by the Plaintiff under protest to the Defendant in the amount of $36,708.10, together with appropriate interest from the date of payment.

2. The Plaintiff, Covington Fabrics, Inc. (hereinafter Covington), is a New York corporation authorized to do business and doing business in South Carolina under the authority of the South Carolina Business Corporation Act. The Plaintiff is a converter of unfinished textile goods. Its principal activities consist of (1) the purchase of unfinished goods, (2) the styling of the goods, (3) the conversion of these goods through independent contractors, (4) the warehousing of the finished goods and, (5) the marketing of the finished goods. A portion of the raw materials are purchased in the United States from wholesalers, some of whom are located in South Carolina, and a portion is purchased overseas and imported through ports in New York City; Norfolk, Virginia and Charleston, South Carolina. The raw materials are first sent to Georgia for cleaning and are then shipped primarily to one of two South Carolina finishing plants for conversion into slipcovers, draperies and upholstery fabrics. The finished goods are then brought to McColl, South Carolina, where Covington maintains a centralized warehousing operation. All of the Plaintiff's finished goods inventory (except samples) are stored at McColl. The executive and administrative sales offices of the Plaintiff are housed in New York City where styles and patterns are designed. The Plaintiff maintains sales offices in Los Angeles and Chicago. Covington employs a sales force of ten (10) salesmen who operate over an area of forty-nine (49) states. Although invoicing and billing is routed through the New York City office, shipments are made from McColl directly to customers who are located throughout the United States. In brief, the Plaintiff engaged in a multistate business which is unitary in nature.

3. The controversy in this action involves the application of the sales factor of the South Carolina income tax apportionment formula. The apportionment formula is used for both corporation income tax and corporation license fee purposes. The formula allocates a portion of the

entire net income (capital stock in the case of the license fee) of certain multistate businesses to this State based on a three-factor average. It is contained in Sections 65-279.3, 65-279.4, 65-279.5 and 65-279.6 of the Code. The three factors used in the apportionment are property, payroll and sales. The Plaintiff has alleged that the application to it of the apportionment formula, more particularly the application of the sales factor, has produced an unreasonable tax result and, as applied to it, is unconstitutional in that it violates both the Commerce Clause of the United States Constitution and the Due Process Clauses of both the South Carolina Constitution and the United States Constitution. The sales factor is contained in Section 65-279.6 of the Code and is determined by the ratio of sales made by the taxpayer during the income tax year which are attributable to this State to the total sales made by the taxpayer everywhere. The questions to be decided in this case are whether the Defendant properly applied the sales factor of the apportionment formula by attributing certain sales to this State and, if the sales factor was correctly applied, did it produce an unconstitutional result.

4. I find that the Defendant, by including sales in which shipment was made from within this State directly to purchasers located in states where the Plaintiff was not taxable, has properly applied the sales factor of the South Carolina apportionment formula. The parties are in agreement that sales should be attributed to this State for the purpose of inclusion in the sales factor of the apportionment formula when the purchaser of the goods is in this State. This is a so-called destination sale. The controversy has arisen from the attribution to South Carolina of certain origin sales; that is, sales in which the goods are shipped from the McColl warehouse to purchasers located in certain other states.

The sales factor provides for the inclusion of destination sales. It also provides for the inclusion of origin sales "when the property is shipped from within this State and the purchaser is the United States Government or **the taxpayer is not taxable in the state of the purchaser.**" From the testimony it is clear that for the sales in controversy,

shipment of the goods was made from within this State. It is therefore necessary to determine whether or not the Plaintiff was taxable in certain states into which the goods were shipped; that is, the state of the purchaser. A state's power to tax interstate business is a question to be determined under Federal law. In its interpretation of the United States Constitution, the Supreme Court has defined certain minimum contacts with a state which must exist before a state can acquire jurisdiction to tax. See *Northwestern States Portland Cement Company v. Minnesota*, 358 U. S. 450, 79 S. Ct. 357. Minimum standards of activity are now defined in Public Law 86-272, the only federal legislation relating to the subject. See 15 U. S. C. A. Section 381. The record shows that the Plaintiff had only minimal contact with states other than South Carolina, New York, California and Illinois. It is the attribution to this State of sales in which shipments were made from McColl directly to purchasers in states other than these four that is in issue. I find that the Plaintiff has offered no evidence to show that it was **taxable** in any states other than these. The Plaintiff's own expert witness has testified that he "doubted" that the Plaintiff could be subjected to tax in any other states. Instead the Plaintiff has argued that whether or not it can be subjected to tax in other states has no bearing on its tax liability to South Carolina. I disagree with the Plaintiff on this point. I conclude that the sales factor is explicit in defining what sales are attributable to this State. An origin sale must meet two criteria: (1) shipment must be made from within South Carolina and, (2) the taxpayer must not be **taxable** in the state of the purchaser.

Not including South Carolina, the Plaintiff made sales to customers located in forty-eight (48) states. I conclude that with the exception of New York, California and Illinois (which did not have an income tax), the Plaintiff was not taxable in any state into which goods were shipped from South Carolina. I base this conclusion on the lack of activities in these states and the fact that these minimal activities did not give these states sufficient contact with the Plaintiff to subject the Plaintiff to a tax liability.

5. The position of the Plaintiff is that Section 65-222.2 of the Code prohibits the inclusion of the origin sales in the sales factor of the apportionment formula and that the Defendant should not have followed the precise statutory mandate contained in Section 65-279.6. The Plaintiff has relied on the language of Section 65-222.2 which states that the income tax of a multistate business should be "imposed upon a base which reasonably represents the proportion of the trade or business carried on within this state". It contends that the application of the sales factor of the apportionment formula contained in Section 65-279.6 of the Code is inconsistent with the provisions of the imposition section contained in Section 65-222.2. From an examination of the record before me in this reference, I find that the application of the apportionment formula has produced a "reasonable" result within the meaning of Section 65-222.2 of the Code.

Sections 65-222.2 and 65-222.6 of the Code were enacted as parts of the "Act Providing for the Determination, Allocation and Apportionment of Income for Tax Purposes". See Sections 2 and 5(c) of Act No. 731, Acts and Joint Resolutions of 1958 at 1574. These sections relating to the same subject are therefore in *pari materia* and must be construed together. In Section (5) of the 1957 Act, the General Assembly specifically provided a method, by means of the apportionment formula, to arrive at what it must have considered to be a "reasonable" apportionment of income. I do not find these sections, now codified as Sections 65-222.2 and 65-279.4 through 65-279.6, to be inconsistent. My conclusion is supported by the language of the South Carolina Supreme Court in the case of *Hertz Corporation v. South Carolina Tax Commission,* 246 S. C. 92, 142 S. E. (2d) 445 (1965). The court in analyzing the provisions of Act No. 731 stated:

> "The purpose of this legislation, as declared * * * is to provide for the imposition of the South Carolina income tax, where the taxpayer is also subject to income tax in other states 'upon a base which reasonably represents the proportion of the trade of business carried on within this State.'"
> * * *
>
> "The legislature apparently considered that the **three factor formula** would be best calculated to attain the **objective of reasonable allocation of income** where the business of the taxpayer is appropriate to its use, and undertook to classify business accordingly. * * *." (Emphasis added.)

Although I will not substitute my judgment for that of the General Assembly in arriving at what portion of the taxpayer's income should be allocated to South Carolina, it is interesting to note that warehousing is an important part of this taxpayer's business. The Plaintiff does no manufacturing and it contracts for the finishing of its raw materials.

6. I conclude that the South Carolina apportionment formula as applied to the Plaintiff is not unconstitutional and that its application violates neither the Constitution of South Carolina nor the Constitution of the United States.

The Plaintiff has alleged that the tax in question violates the Due Process Clause as a taking without due process of law, and that it violates the Commerce Clause in that it is imposed on interstate business beyond the jurisdiction of this State. In *Wisconsin v. J. C. Penney Co.,* 311 U. S. 435, 61 S. Ct. 246, p. 250 (1940), the Supreme Court stated:

> "* * *. That test is whether property was taken without due process of law, or, if paraphrase we must, whether the taxing power exerted by the state bears fiscal relation to protection, opportunities, and benefits given by the state. The simple but controlling question is whether the state has given anything for which it can ask return. The substantial privilege of carrying on business in Wisconsin, which has here been given, clearly supports the tax, and the state has not given the less merely because it has conditioned the demand of the exaction upon happenings outside its own borders. The fact that a tax is contingent upon events

> brought to pass without a state does not destroy the *nexus* between such a tax and transactions within a state for which the tax is an exaction. * * *."

I find that activities of the Plaintiff in South Carolina are clearly substantial as compared to their over-all operations. I further find that the tax imposed bears fiscal relation to the protection and benefits given by this State. South Carolina has taxed approximately 55% of the Plaintiff's total income. I conclude that the burden is on the Plaintiff to show that the apportionment formula resulted in extraterritorial values being taxed, and the United States Supreme Court has stated that this burden of proof must be met by "clear and cogent evidence". See *Buller Bros. v. McColgan,* 315 U. S. 501, 62 S. Ct. 701 (1942), and *Norfolk and Western Ry. Co. v. North Carolina,* 297 U. S. 682, 56 S. Ct. 625. This burden of proof was met in the case of *Hans Rees' Sons v. State of North Carolina,* 283 U. S. 123, 51 S. Ct. 385, on which the Plaintiff so heavily relies. However, I find that the Plaintiff has not brought itself within the rationale of that case. The South Carolina Supreme Court considered the *Hans Rees'* decision in *Mercury Motor Express, Inc. v. South Carolina Tax Commission,* 244 S. C. 134, 135 S. E. (2d) 756, and Mr. Justice Bussey stated:

> "There (in *Hans Rees'*) the State of North Carolina applied its proportionate property value formula to determine the taxable net income of a manufacturing concern in that state. The taxpayer contended **that it was not engaged in a unitary business;** that its net income derived from activities in North Carolina was determinable without the necessity of resorting to any proportionate formula; and offered evidence of the effect that the portion of its net income attributable to activities in the State of North Carolina was some seventeen per cent, whereas, the application of the formula allocated to the State of North Carolina from sixty-six per cent to eighty-five per cent of the net income of the taxpayer." (Emphasis added.)

I find that the Plaintiff operates a unitary business. I also find that it has not attempted to separately account for the portion of its income derived from South Carolina activities and has introduced little or no evidence breaking its business into component parts. In the case of *Maxwell v. Kent-Coffey Manufacturing Co.,* 204 N. C. 365, 168 S. E. 397, Aff'd *per curiam* 291 U. S. 642, 54 S. Ct. 437, relied on by our court in *Mercury Motor Express,* the North Carolina Supreme Court stated that in order to meet the criteria of the *Hans Rees'* decision, evidence must be introduced showing the influence of each factor of the business in producing income. No such evidence has been introduced. Based on the evidence presented, I find that the Plaintiff has not met the burden of proof required to show that the South Carolina apportionment formula has allocated an arbitrary or unreasonable amount of its income to this State and I further find that it has not shown that the allocation has taxed extraterritorial values.

In its Brief, the Plaintiff has stated that the South Carolina apportionment formula has subjected it to the risk of multiple taxation. I find that the Plaintiff has offered no evidence that interstate commerce has been burdened by multiple taxation. Instead I find from the evidence presented that for the tax years in question, all states combined did not tax more than 85% of Covington's income. The decisions of the United States Supreme Court hold, and I conclude, that the burden is on the taxpayer to show that it has been actually subjected to multiple taxation. See *General Motors Corporation v. Washington,* 337 U. S. 436 (1964). It is therefore not necessary to pass on the "risk" of multiple taxation. However, it should be noted that the South Carolina apportionment formula corresponds to that contained in the *Uniform Division of Income for Tax Purposes Act,* Section 9, *et seq.,* 9A Uniform Laws Annotated 449, which has been adopted in a number of states. The sales factor contained in the South Carolina apportionment formula is substantially identical to that contained in Section 16 of the Uniform Act. The Uniform Act was, of course, designed to prevent the possibility of double taxation.

A great deal of evidence was presented and arguments were put forth by both Plaintiff and Defendant on the question of where title passed and sales took place. Since that time, the South Carolina Supreme Court handed down the case of *United States Steel Corporation v. South Carolina Tax Commission,* 259 S. C. 153, 191 S. E. (2d) 9. In that case the court said that for the purpose of including sales in the sales factor of the apportionment formula "the technical situs at which a sale is confirmed, controlling for other legal purposes, is irrelevant here". We are concerned here with what sales are attributed to South Carolina for income tax and license fee apportionment purposes. This is not a sales tax and South Carolina has not attempted to tax these sales. I conclude that the question of passage of title is not controlling here.

CONCLUSION

I therefore conclude that the inclusion in the sales factor of the apportionment formula of sales in which shipment was made from within this State directly to purchasers in states where the Plaintiff could not have been subjected to taxation was proper. I further conclude that the attribution of these sales to South Carolina for income tax and license fee apportionment did not violate the provisions of either the South Carolina or United States Constitutions.

Respectfully submitted,

/s/ OWENS T. COBB, JR.,
As Master in Equity for
Richland County.

APPENDIX D

ART. I, § 8 CONSTITUTION OF THE UNITED STATES

§ 8. Powers of Congress.

The Congress shall have power . . .

To regulate commerce with foreign nations, and among the several states, and with the Indian tribes; . . .

And

To make all laws which shall be necessary and proper for carrying into execution the foregoing powers, and all other powers vested by this Constitution in the government of the United States, or in any department or officer thereof.

* * *

APPENDIX E

CONSTITUTION OF THE UNITED STATES

ARTICLE XIV.

§ 1. Citizenship rights not to be abridged by states.

All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the state wherein they reside. No state shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any state deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.

APPENDIX F

Public Law 86-272

15 U. S. C. § 381. Imposition of net income tax—Minimum Standards

(a) No State, or political subdivision thereof, shall have power to impose, for any taxable year ending after September 14, 1959, a net income tax on the income derived within such State by any person from interstate commerce if the only business activities within such State

by or on behalf of such person during such taxable year are either, or both, of the following:

(1) the solicitation of orders by such person, or his representative, in such State for sales of tangible personal property, which orders are sent outside the State for approval or rejection, and, if approved, are filled by shipment or delivery from a point outside the State; and

(2) the solicitation of orders by such person, or his representative, in such State in the name of or for the benefit of a prospective customer of such person, if orders by such customer to such person to enable such customer to fill orders resulting from such solicitation are orders described in paragraph (1).

Domestic corporations; persons domiciled in or residents of a State

(b) The provisions of subsection (a) of this section shall not apply to the imposition of a net income tax by any State, or political subdivision thereof, with respect to—

(1) any corporation which is incorporated under the laws of such State; or

(2) any individual who, under the laws of such State, is domiciled in, or a resident of, such State.

Sales or solicitation of orders for sales by independent contractors

(c) For purposes of subsection (a) of this section, a person shall not be considered to have engaged in business activities within a State during any taxable year merely by reason of sales in such State, or the solicitation of orders for sales in such State, of tangible personal property on behalf of such person by one or more independent contractors, or by reason of the maintenance, of an office in such State by one or more independent contractors whose activities on behalf of such person in such State consist solely of making sales, or soliciting orders for sales, of tangible personal property.

Definitions

(d) For purposes of this section—

(1) the term "independent contractor" means a commission agent, broker, or other independent contractor who is engaged in selling, or solicting orders for the sale of, tangible personal property for more than one principal and who holds himself out as such in the regular course of his business activities; and

(2) the term "representative" does not include an independent contractor.

Pub. L. 86-272, Title I, § 101, Sept. 14, 1959, 73 Stat. 555.

§ 382. Assessment of net income taxes; limitation; collection

(a) No State, or political subdivision thereof, shall have power to assess, after September 14, 1959, any net income tax which was imposed by such State or political subdivision, as the case may be, for any taxable year ending on or before such date, on the income derived within such State by any person from interstate commerce, if the imposition of such tax for a taxable year ending after such date is prohibited by section 381 of this title.

(b) The provisions of subsection (a) of this section shall not be construed—

(1) to invalidate the collection, on or before September 14, 1959, of any net income tax imposed for a taxable year ending on or before such date, or

(2) to prohibit the collection, after September 14, 1959, of any net income tax which was assessed on or before such date for a taxable year ending on or before such date.

§ 383. Definition

For purposes of this chapter, the term "net income tax" means any tax imposed on, or measured by, net income.

§ 384. Separability provision

If any provision of this chapter or the application of such provision to any person or circumstance is held invalid, the remainder of this chapter or the application of

such provision to persons or circumstances other than those to which it is held invalid, shall not be affected thereby.

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APPENDIX G

South Carolina Code of Laws (1962)

§ 65-222. **Tax on corporations.**—Every corporation organized under the laws of this State, whose entire business is transacted or conducted within this State, shall make a return and shall pay annually an income tax equivalent to five per cent of the entire net income received by such corporation during the income tax year, and except as otherwise provided, every corporation organized under the laws of this State, doing or transacting business partly within and partly without this State, shall make a return and shall pay annually an income tax equivalent to five per cent of proportion of its entire net income, to be determined as provided in this chapter, and except as otherwise provided, every foreign corporation transacting, conducting, doing business or having an income within the jurisdiction of this State, whether or not such corporation be engaged in or the income derived from intrastate, interstate, or foreign commerce, shall make a return and shall pay annually an income tax equivalent to five per cent of a proportion of its entire net income, to be determined as provided in this chapter. The terms "*transacting,*" "*conducting,*" or "*doing business,*" as used in this section shall include the engaging in or the transacting of any activity in this State for the purpose of financial profit or gain.

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§ 65-222.2. **Tax on businesses conducted partly within and partly without the State.**—If any taxpayer, except those defined in § 65-256, is transacting or conducting his business partly within and partly without this State, the income tax as provided in this chapter shall be imposed upon a base which reasonably represents the proportion of the trade or business carried on within this State. The taxpayer subject to taxation under this section shall be deemed to have been transacting or conducting his business

partly within and partly without the State if such taxpayer is subject to a net income tax or a franchise tax measured by net income in any other state, the District of Columbia, a territory or possession of the United States, or any foreign country, or would be subject to the net income tax in any other such taxing jurisdiction if such other taxing jurisdiction adopted the net income tax laws of this State. *Provided,* that nothing herein shall operate to deny any taxpayer affected by this section and §§ 65-222, 65-222.1, and 65-279 to 65-279.11 the benefits of § 65-259 (12) where such taxpayer suffers a net loss, but as to the apportionment of net operating losses carried forward, the provisions of those sections apply as if the taxpayer had a net income. (1958 (50) 1574; 1959 (51) 363.)

* * *

§ 65-279.6. **Same; ratio for sales.**—The ratio of sales made by such taxpayer during the income year which are attributable to this State to the total sales made by such taxpayer everywhere during the income year, and for purposes of this article, sales attributable to this State shall be all sales where the goods, merchandise, or property is received in this State by a purchaser, other than the United States Government. In the case of delivery of goods by common carrier, or by other means of transportation, including transportation by the purchaser, the place at which the goods are ultimately received after all transportation has been completed shall be considered as the place at which the goods are received by the purchaser. Direct delivery into this State by the taxpayer to a person or firm designated by a purchaser from within or without the State shall constitute delivery to the purchaser in this State. Sales are attributable to this State when the property is shipped from within this State and the purchaser is the United States Government or the taxpayer is not taxable in the state of the purchaser. The word "*sales*" as used in this article shall be construed to include rentals of tangible personal property the rentals from which are not separately allocated under this article. Such rentals to be attributed to this State if the property is located in this State. Sales of intangible personal property shall be

attributable to this State if the entire income producing activity is within this State, or based on costs of performance the greater proportion thereof is performed within this State. (1958 (50 1574; 1959 (51) 363.)

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§ 65-602. **Annual reports to be filed by corporations and cooperatives; exemption of cooperatives from tax.**—Every corporation organized under the laws of South Carolina to do business for profit and every corporation organized to do business under the laws of any other state, territory or country and qualified to do business in South Carolina and any other corporation required by § 65-222 to file income tax returns shall, in addition to any and all other requirements of law, make a report annually to the Tax Commission on or before the fifteenth day of the third month next after the preceding income year in such form as may be prescribed by the Tax Commission containing such information and facts as the Commission may require for the administration of the provisions of this chapter.

Cooperative organizations and corporations organized under chapters 14, 15 or 16 of Title 12 shall file reports required by this section, but shall be exempt from the tax levied in § 65-606.

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§ 65-606. **License tax imposed on corporations generally; rate; when payable.**—In addition to any and all other license taxes or fees or taxes of whatever kind, every corporation required to file a report by § 65-602, except such corporations as are enumerated in § 65-608, shall pay to the Commission, at the time of filing the report required by § 65-602, an annual license fee of one mill upon each dollar paid to the capital stock and paid in as surplus of said corporation as shown by the records of the corporation on the first day of the income year next preceding the date of filing the report. In no case shall the license fee provided for by this section be less than ten dollars. The license fee provided for by this section shall be paid at the time of filing the report pursuant to the provisions of

§ 65-602, on or before the fifteenth day of the third month next after the preceding income year.

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APPENDIX H

NOTICE OF APPEAL TO THE SUPREME COURT OF THE UNITED STATES

Notice is hereby given that Covington Fabrics Corp., Appellant above named, hereby appeals to the Supreme Court of the United States from the final judgment of the Supreme Court of the State of South Carolina, by Opinion No. 19968, filed March 10, 1975.

This appeal is taken pursuant to 28 U. S. C. 1257 (2).

JAMES M. WINDHAM,
Counsel for Appellant.

May 16, 1975

CERTIFICATE OF SERVICE

I hereby certify that service of the foregoing notice of appeal has been mailed, postage prepaid, to John C. von Lehe, Esquire, Assistant Attorney General, South Carolina Tax Commission, P. O. Box 125, Columbia, South Carolina, Counsel for Appellee, this 16th day of May, 1975. I further certify that all parties required to be served have been served.

JAMES M. WINDHAM,
Counsel for Appellant.